Australian Government

Austrade

# Inquiry by the Senate Foreign Affairs, Defence and Trade References Committee into the Importance of the Indian Ocean rim for Australia's foreign, trade and defence policy

Submission by the Australian Trade Commission

**TERMS OF REFERENCE**

The following matter be referred to the Senate Foreign Affairs, Defence and Trade References Committee for inquiry and report by 1 November 2012:

The importance of the Indian Ocean rim for Australia's foreign, trade and defence policy, with particular reference to:

(a) trade and tourism opportunities for Australia, including the role of free trade agreements;

(b) Australian mineral exports, including competition and synergies in the region;

(c) strategic developments in the Indian Ocean, including growing naval influences and defence postures and their implications for Australia and the region more generally;

(d) the Indian Ocean Rim Association and any other relevant bodies and their future directions; and

(e) other relevant matters.

# Submission by the Australian Trade Commission

## The Indian Ocean Rim region: Definition

The Indian Ocean Rim (IOR) comprises up to 48 countries spread across Africa, the Middle East, South Asia, South-East Asia and Australia[1]. IOR nations are a heterogeneous group, comprising an extremely diverse range of developed, developing and under-developed states (from Singapore to Malawi). Under this definition the IOR represents 2.6 billion people or 39 per cent of the world's population[2]. Importantly, the Indian Ocean encompasses major commercial sea routes, and is emerging as a region of great strategic significance. Much of the world's energy trade transits across the Indian Ocean, including approximately two-thirds of Persian Gulf oil exports to Asia[3].

## Rapid emergence of the middle class in the Indian Ocean Rim will be a defining trend of the 21st century

The IOR will undergo a period of profound development in the next 20 years, characterised by an extraordinary increase in the breadth of participation by its population in the broader global economy. The major macroeconomic trend over this period in the region will be the surge in its middle class population, driven by a combination of sustained increases in both population and GDP per capita.

The OECD estimates that by 2030 the global middle class will grow from 1.8 to 4.9 billion people[4]. The vast proportion of these new middle class consumers will come from India and China, but also from the ASEAN states[5]. India's middle class population is projected to reach 583 million by 2025[6], and it could potentially have over 1 billion middle class consumers by 2039[7]. India's rapid economic development will be paralleled by similar development in Africa and the Middle East.

Africa's population is also swelling rapidly, offering an array of opportunities and challenges. Since 2000 the continent's population has expanded by 200 million to exceed one billion. Future growth projections are even more striking; population growth for the next decade could average 2.2 per cent, compared to 0.9 per cent in Asia. It is estimated that around 150 million Africans have entered the middle class since 1990, and a further 40 million households will become middle class by 2015. Kenya, Mozambique, Tanzania and South Africa are key African nations in the IOR which illustrate this trend.

Three prominent opportunities are likely to be driven by these developments.

- First, when coupled with robust economic growth, population growth will support the emergence of the region's consumer base—providing support to local firms, creating economic opportunities, and inspiring increasingly diversified foreign investment.

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[1] Australian Strategic Policy Institute, *Our Western front: Australia and the Indian Ocean*, March 2010.
[2] Australian Strategic Policy Institute, already cited, see Footnote 1.
[3] Australian Strategic Policy Institute, already cited, see Footnote 1.
[4] OECD Development Centre Working paper No. 285, *The Emerging Middle Class in Developing Countries*, January 2010.
[5] OECD Development Centre, already cited, see Footnote 4.
[6] A 2007 McKinsey Institute Report referred to by OECD Development Centre, already cited, see Footnote 4.
[7] OECD Development Centre, already cited, see Footnote 4.

- Second, for countries able to provide the necessary institutional support, a youthful and growing population has the potential to yield a demographic dividend, which, if leveraged effectively, will open new frontiers in the services and manufacturing sectors.
- A third key macroeconomic trend in the region will be intense urbanisation. Urban demand centres and the emergence of mega-cities (cities with populations of 10 million or more) will increasingly be focal points of economic activity in the IOR. Increasingly higher proportions of the population will live in cities, and urban centres will also account for higher proportions of GDP. For example, urban India could generate approximately 70 per cent of India's GDP by 2030[8], and by 2030 Mumbai and Delhi are likely to be among the five largest cities in the world[9].

## Implications for Australia

These macro trends will create enormous commercial opportunity for Australia across the region in coming years. There will be exponentially increased demand for food, water, resources and energy, driven by rapid growth in the region (in particular, but not exclusively, led by India). The rapid expansion of a highly urbanised middle class will also lead to a sharp increase in consumer demand for goods and services.

This regional macro demand aligns closely with Australia's major strengths in agribusiness, mining and energy, and given our proximity to the region represents a tremendous opportunity to deepen our trade and investment relationship with the region. Australian firms also will see increasing opportunities to invest and innovate in these markets to capture improvements in resource (land, water, energy and food) productivity, as well as increasing supply of these goods from Australia.

*Agribusiness*

Agribusiness and land ownership are sensitive issues for many countries across the region. Price indices reflect the importance of food in daily consumption expenditure, and its vulnerabilities to policy changes, biofuel production, energy prices, weather, economic growth and changing diets, exchange rate movements and speculation.[10]

For example, according to India's Planning Commission, the country can feed itself but nutritional levels are below UN averages, wastage can be as high as 30-60 per cent and farming is dominated by small unproductive land holdings and herds. Further the country's water table has been seriously degraded through drought, overuse and rising salinity.

Africa's agricultural sector has persistently underperformed for much of the past half century—having been a net food exporter in the early 1960s, Africa is now a net importer. Between 1998 and 2008some estimate that the number of hungry people in Sub-Saharan Africa (SSA) increased by 20 per cent. And, between 1967 and 2007, farm output per person in SSA fell by one-quarter, even while it doubled in South Asia and tripled in East Asia.

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[8] McKinsey Global Institute, *India's urban awakening: Building inclusive cities, sustaining economic growth*, April 2010.
[9] McKinsey Global Institute, already cited, see Footnote 8.
[10] Westhoff, P., *The Economics of Food*, FT Press, 2010, New Jersey.

India, China, Saudi Arabia and the Gulf countries are all leasing or acquiring fertile land in East Africa for contract farming notably in Ethiopia, Madagascar, Kenya and Mozambique. Some estimates assess that between 50 and 60 million hectares of land in SSA has been purchased or leased since 2001. The majority of land leasing agreements are structured on a government-to-government basis.[11]

There are therefore emerging investment opportunities in agribusiness across much of South Asia, the Gulf and East Africa where countries are seeking pulses and grains, quality processed foods including halal compliant food stuffs, new farming skills, agricultural technologies including seed resilience, irrigation products and technologies (including water usage) and critically, assistance with improving logistics and supply chains. Agricultural supply chain improvement is needed by many countries across the region (particularly India, and also East Africa) to maximise the output of agriculture, offering opportunities for Australian firms with capabilities in this area. In most cases sustained export will require investment in the region and local partners to overcome significant tariff and non-tariff barriers, particularly related to food stuffs.

*Mining and energy*

Sources of energy supply and demand needs vary greatly across the region - from self-sufficiency of crude oil in the Gulf to oil dependence in India and newly discovered reserves in northern Kenya.[12] East Africa is known to have large untapped mineral deposits and energy reserves, and continues to attract prospective mining and exploration companies from around the world, including a large and growing Australian mining presence.[13] The countries within the region are however at different stages of realising this potential. Most of these minerals still remain untapped due to inadequate knowledge on their status, economic viability and appropriate mining technologies.

For example, Kenya's mining sector is largely under-explored, with the mining sector currently contributing less than 1 per cent of GDP. Minerals found in Kenya include soda ash, fluorspar, limestone, barite, titanium, lead, nickel, copper, zinc gold, coal, iron ore, salt, dimension stone, silica sand, soapstone, manganese chromite, pyrite, rare earth elements and phyrochore. However, only approximately 10 per cent of Kenya's territory has been covered in recent airborne geophysical surveys.[14]

This sector will increasingly offer Australian firms opportunities in mineral exploration, mining software, mining processing technologies, mining equipment, engineering services, and mining education and training services.

*Other sectors*

Other growth sectors across the region include health and medical, advanced manufacturing, tourism and hospitality, infrastructure development, education, and defence and security,

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[11] *The five trends powering Africa's enduring allure: Trend 4 Africa's dormant resources potential*, Standard Bank, October 7, 2012, Johannesburg.
[12] 'Kenya oil discovery after Tullow Oil drilling'; http://www.bbc.co.uk/news/world-africa-17513488, accessed March 28, 2012.
[13] Future Directions, *Australia and the New Great Game in East Africa, May 3, 2011.*
[14] Draft Kenya Mining Policy, September 5, 2011, http://www.kenyachambermines.com/publications/documents#9, accessed March 28, 2012.

again representing an opportunity for Australian firms. Rapidly growing demand for services (including education, professional services, and financial services) will also generate new opportunities.

**Austrade's agenda in the Indian Ocean Rim**

Austrade is well positioned to assist Australian companies to take advantage of the emerging opportunities in the IOR. Austrade has recently completed a major review, enhancing its capability (within current resources) to identify and prioritise opportunities for Australian firms in developing and high-growth markets, including many in the IOR states. Austrade's new organisational alignment emphasises market types rather than regions, with the Growth and Emerging markets grouping covering most of the IOR countries (with the exception of ASEAN states) – this new focus will assist Austrade to better capture opportunities in this region for Australian firms.

Overall, Austrade's value-add to internationally ready Australian firms and education providers in this region is:

a) the ability to identify and assess business opportunities in IOR markets;
b) providing advice on doing business in these markets;
c) networks of key decision makers, customers and contacts;
d) market information and insight; and
e) the ability to leverage the 'badge of government' for the benefit of Australia.

Specifically, Austrade will continue to provide targeted trade facilitation and development activities across these markets, where:

a) language and business culture, as well as genuine security concerns and perceptions of doing business can prove a barrier;
b) there is less openness of regulatory frameworks and transparency of business processes – governance, transparency and business ethics are all issues across the IOR region;
c) there are difficulties accessing distribution channels and commercial connections; and
d) the value of the 'badge of government' is highest.

*Trade*

Australia has a competitive advantage in mining equipment, technology and services and agribusiness, however other sectors also have the potential to capture significant emerging opportunities in the IOR. For example, Australia has the potential to be a key supplier of liquefied natural gas to the IOR. Rapidly growing infrastructure demand across the IOR will also present multiple and challenging opportunities for internationally ready Australian firms. Austrade can play a role in seeking to ensure that Australian firms are aligned to and aware of the commercial opportunities in this sector, as well as the trade routes across the region.

Austrade will also seek to encourage the development of strategic capabilities that can deliver a particularly high value add in equipment, technology and services exports to the region. New business opportunities could be fostered by increased leverage of the Australian Unlimited brand to market and reinforce Australia's strengths in the region. Austrade can also

potentially assist by looking for opportunities to market and expand Australia's excellence in sourcing and delivering skills training in the IOR.

Austrade also potentially has a role to play in encouraging greater interest in the Australian business community in the region by:

- demonstrating the benefits of trade and investment by highlighting models and practical examples of where Australian companies, including small and medium companies, have achieved success across the IOR; and
- sharing relevant research such as analysis on commercial opportunities in the region.

*Investment*

Whilst the primary focus for Austrade in the IOR will be facilitating trade, attracting inward investment will also form part of Austrade's agenda for the IOR, as will facilitating outwards investment. Austrade can also assist in the attraction of inward investment from the region in line with Australian government priorities. Foreign Direct Investment demand is high regionally and growing quickly. For example, infrastructure investment in India has averaged 7 per cent of GDP in recent years, potentially growing to 9-10 per cent of GDP this decade, and the African Development Bank Group estimates the infrastructure financing deficit for Africa to be US$93 billion per year until 2020. However regulatory barriers and ease of investment remain a challenge in many countries in the region – for Australian firms willing to invest in critical sectors there will be increased opportunities.

*Education*

The export of education services is a key element of Austrade's engagement with the IOR. There is growing demand from the region to address education, training and skills gaps (for example, the Indian government's stated aim of skilling 500 million people by 2020) and Austrade can play a valuable role in promoting the quality and accessibility of Australian educational services across the IOR. Austrade will also continue to work with its stakeholders in higher education, vocational and education training to utilise Australia's world-class education expertise to build and deliver in-market education and training capability where it is most needed in the region, and to assist Governments meeting their skills targets.

Attachment A

## Austrade's overseas staff headcount and locations in Indian Ocean Rim countries (as at 31 December 2011)

| Sub Region/Location | A-Based staff overseas | Overseas employed staff | Total |
|---|---|---|---|
| **Middle East** | | | |
| Abu Dhabi | 1 | 1 | 2 |
| Amman | 1 | 3 | 4 |
| Qatar (Doha) | 0 | 1 | 1 |
| Dubai | 2 | 15 | 17 |
| Jeddah | 0 | 1 | 1 |
| Kuwait | 0 | 0 | 0 |
| Oman (Muscat) | 0 | 1 | 1 |
| Riyadh | 1 | 5 | 6 |
| **Sub-total** | **5** | **27** | **32** |
| **Sub-Saharan** | | | |
| Johannesburg | 1 | 4 | 5 |
| Nairobi | 0 | 1 | 1 |
| Port Louis | 0 | 1 | 1 |
| **Sub-total** | **1** | **6** | **7** |
| **South Asia** | | | |
| Ahmedabad | 0 | 1 | 1 |
| Bangalore | 0 | 2 | 2 |
| Chandigarh | 0 | 1 | 1 |
| Chennai | 1 | 8 | 9 |
| Colombo | 0 | 2 | 2 |
| Dhaka | 0 | 2 | 2 |
| Hyderabad | 0 | 2 | 2 |
| Islamabad | 0 | 1 | 1 |
| Jaipur | 0 | 1 | 1 |
| Karachi | 0 | 1 | 1 |
| Kochi | 0 | 1 | 1 |
| Kolkata | 0 | 2 | 2 |
| Lahore | 0 | 1 | 1 |
| Mumbai | 2 | 12 | 14 |
| New Delhi | 3 | 16 | 19 |
| Pune | 0 | 1 | 1 |
| **Sub-total** | **6** | **54** | **60** |
| **South-East Asia** | | | |
| Bangkok | 2 | 21 | 23 |
| Jakarta | 3 | 22 | 25 |
| Kuala Lumpur | 2 | 15 | 17 |
| Singapore | 2 | 15 | 17 |
| **Sub-total** | **9** | **73** | **82** |
| | | | |
| **TOTAL** | **21** | **160** | **181** |